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Snarr Advertising Inc v. The Utah State Tax Commission : Brief of Appellant

Utah Supreme Court

DOCKET NO. 10808 Pro

IN THE

SUPREME COURT
OF THE
STATE OF UTAH

SNARR ADVERTISING, INC.,
a corporation,

Plaintiff,

- vs. -

THE UTAH STATE TAX COMMISSION,

Defendant.

Case No. 10808

PLAINTIFF'S BRIEF

ORIGINAL PROCEEDINGS ON A WRIT OF CERTIORARI TO THE TAX COMMISSION OF THE STATE OF UTAH

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TABLE OF CONTENTS

CASES CITED

TABLE OF CONTENTS—Continued

REGULATIONS CITED

TABLE OF CONTENTS—Continued

Page

STATUTES CITED

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STATEMENT OF THE NATURE OF THE CASE

This action was commenced by Plaintiff by the filing of two petitions before the State Tax Commission. The first of these, filed February 3, 1965, petitioned for the refund of Sales Tax erroneously and illegally collected. (R. 1). The second, filed on May 21, 1965, petitioned for a review and correction of a Tax Commission Audit concerning various aspects of Plaintiff's sales tax liability. (R. 5). The two petitions were consolidated by stipulation of the parties and the sole issue considered by the Commission and before this Court on certiorari was stipulated to be as follows:

> "The sole issue to be resolved in this proceeding is the proprietory of imposing sales tax upon the receipts from advertising upon outdoor advertising signs and bill boards." (R. 11)

DISPOSITION IN TAX COMMISSION

A hearing was held before the Commission on August 25, 1965, and the parties entered into a stipulation respecting certain factual and procedural matters on February 21, 1966. On October 25, 1966, the Commission issued its decision which sustained sales taxation of outdoor advertising receipts and thus denied Petitioner's claim for refund and affirmed the deficiency assessment.

RELIEF SOUGHT ON APPEAL

The plaintiff seeks a reversal of the decision of the State Tax Commission as a matter of law.

STATEMENT OF FACTS

The pertinent facts are contained in a stipulation (R. 10-12) and in a transcript of hearing. (R. 13-110). There has not been, in the previous proceedings in this matter, any particular dispute with regard to the applicable facts. Rather, as will appear in argument hereinafter, the differences have arisen from the interpretation, relevancy, and legal significance of the undisputed facts. Since sales taxation, as a legal proposition, must rest basically upon the concise facts of the transaction involved, the following facts concerning the nature of the plaintiff's business and the transactions between plaintiff and its various customers are of significance:

The Nature of the Plaintiff's Business.

Plaintiff is in the outdoor advertising business. Its prime function is to place advertisements for its clients, and its business is generally restricted to the medium of outdoor advertising. (R. 63). This business is carried on throughout the western states, and, within Utah, plaintiff places only painted signs as opposed to posters. (R. 64).

The plaintiff is contacted by its clients in one of two ways: the company wishing to advertise contacts the plaintiff directly (R. 77), or, plaintiff is contacted by an advertising agency, hired by the company wishing to advertise. (R. 77). Plaintiff employs from four to six salesmen within this area who perform the function of meeting with the clients, discussing the nature of the advertising desired, and the type of coverage required. (R. 65). After the initial contacts, the advertiser is put in touch with the plaintiff's art department to further refine the type of advertising program to be employed. The art department, after such consultation, compiles a written presentation of the suggested advertising program. (R. 66). This is reviewed by and discussed with the client, and is subject to his approval. (R. 66). After the client approves of the program, he signs an "art work approval" form. (R. 200).

The next step is the selection and acquisition, if necessary, of real property locations whereon the advertising structures will be placed. In some instances, plaintiff may have under existing lease a location and sign structure which are suitable for the clients needs. (R. 66). In others, however, where no location and structure are available, the petitioner must acquire a suitable location and place a structure thereon. (R. 66).

The real property required for these locations is leased from the land owner. (R. 66). A standard lease agreement used by plaintiff in this regard was admitted as an exhibit. (R. 199). As may be observed from such lease, the term is for a period of years, with a right of renewal in plaintiff. The lease further provides that should the property involved loose its advertising value, the plaintiff has the right to terminate the lease upon five days written notice. (R. 199, Paragraph 5).

After the location is selected, and acquired if necessary, the advertising client inspects the location and signifies his approval on a form admitted as an exhibit before the Tax Commission. (R. 201). After the advertising presentation, the location and price have been agreed upon, the final agreement between the advertising client and the plaintiff is executed. The standard agreement used in this regard was admitted as an exhibit in the proceedings below. (R. 203). Paragraph 4 of the agreement provides that plaintiff must maintain the displays in good condition, and that the advertiser may change the display at any time during the term of the agreement at its expense. Under paragraph 5 of the agreement, plaintiff retains the right to move the advertising display to different locations if the original location looses advertising value. Moreover, plaintiff is required to maintain such signs at its expense.

After the execution of the agreement, plaintiff proceeds with the painting of the advertising panel to be used, the construction of the sign sructure (in the event that there is not one available), and the placement of the advertising panel on the structure. During the term of the agreement thereafter, plaintiff maintains the displays and

has the right and obligation to relocate the displays on new locations and structures, in the event that the advertising value of the original structure is diminished, such as by the re-routing of highways. (R. 203).

The Cost to the Advertiser.

Mr. Floyd Moon, Comptroller for the plaintiff, testified that the price for plaintiff's services depends upon "the service the particular client desires" (R. 70), but the criteria involved are the size of the advertisement, the location where the display is to be placed, and the services performed by the plaintiff. (R. 70). A representative hypothetical situation was discussed by Mr. Moon: Assuming that a client wanted three signs in three locations, with the agreement to run for a four year period, Mr. Moon testified that a typical price would be $100.00 per month, or $4,800.00 over the four year period. (R. 71). Such gross income to plaintiff would cover all the costs associated with the provision of the advertising services and placement of the displays, and "hopefully" some profit would be left over at the end. Mr. Moon testified the costs involved might be broken down as follows:

Materials for sign construction	5%
Labor for sign painting and construction	5%
Positioning of sign structure	5%
Total cost for material, labor, and positioning	15%

The remaining 85% of the costs is broken down into a number of various factors including cost of the location paid to the landowner, cost in acquiring the location, electrification and lighting of the structure, rotation of advertisements and structures from place to place in order to keep the advertiser's message before the traveling public,

maintenance of signs throughout the period of the agreement, sales services, and artistic services. (R. 72 thr. 77). The typical sign structure itself, divorced from the various services involved, costs on the average of $100.00. (R. 77). This is not a significant factor in determination of the ultimate price, since matters such as location, length of service, creative services, re-location and maintenance are more important. (R. 78).

The Relationship Between Plaintiff and its Clients.

At the hearing for the Tax Commission, a number of plaintiff's customers testified concerning the relationship between themselves and plaintiff in the placement of outdoor advertising. Typical of such testimony was that of Mr. Glen E. Lee of Terminex Company, who is the officer in charge of that company's advertising program. (R. 34). With regard to the reason for advertising by the company, Mr. Lee stated as follows:

> "The purpose of it is to get our message, our name, before the public."

In conjunction with this purpose, as an advertiser, Terminex does not differentiate between the various advertising media. In the words of Mr. Lee:

> "So far as we are concerned, we see no difference between newspaper, radio, telephone pages or outdoor advertising. Our purpose is to get our message before the public. We pay for getting this done and in no wise have we been taxed in connection with any of this." (R. 35)

Another witness, Joseph S. Francom, spoke from the standpoint of the advertising agency. He stated that as an advertising agency, his company is interested merely in

exposing his client's products to the public. He analyzed the problem as follows:

> "There is no difference as far as that is concerned. The television company bills their television client and we lease or rent or buy from them a certain number of spots or programs which we use. The highways sign company builds a lot of highway signs. We don't own them. *We have nothing to do with them as far as ownership is concerned.* All we do is lease the privilege to use that sign for three years or four years, whatever the period may me. If the sign falls down or breaks up, that is their problem, not the advertisers or the advertising agency. All we do is lease the space." (R. 54).

Mr. Francom further stated:

> "We have nothing to do with the property. We have nothing to do with the structure itself." (R. 56).

And, finally, Mr. Francom noted that he did not feel, as a client and contracting party of the Petitioner, that he had any proprietory interest whatsoever in the Petitioner's signs. (R. 61).

To the same effect was the testimony of Mr. E. S. Hallem, owner of the E. S. Hallem Advertising Agency. (R. 92). He testified that the only interest he has in obtaining advertising services from any media is that the media will best serve the needs of his clients. He said:

> "We don't care whether it is outdoor billboards or television commercials. We are only interested in the results."

When asked whether or not he felt that the advertiser had

any proprietory interest in the personal property involved in billboard signs, he answered as folows:

> "No, absolutely not, because when we buy a sign or a space in the paper we don't care how the thing is produced. We don't care what they do with it. We enter into a contract with the paper for say one issue. With the outdoor people for one year or three years. At the end of this time when our contract is fulfilled and we have paid them, we don't care what they do with the sign. The only thing that we are interested in is that they maintain it and as Mr. Moon has testified we watch them to see that they move the sign to the different locations. This is their responsibility. We are not buying the sign or location. Absolutely not."

Mr. Hallem also stated emphatically that he has no interest whatsoever in the cost of the sign structure involved. (R. 96). Rather, he noted:

> "What I am interested in is the quality of the work and how they perform it, how they reproduce our art work. We don't care about their real estate problems." (R. 96).

Of similar content was the testimony of Mr. Francis Anderson, responsibile for the advertising of Beneficial Life Insurance Company. (R. 100). He stated that all he was interested in is seeing that the product was exposed to the public. He considered that as a client he had no propriety interest whatsoever in the tangible personal property involved in the sign structure. (R. 102). Nor did he consider that the cost or value of the structure was relevant in determining the desirability of placing outdoor advertising. (R. 102). When asked if he assumed the possession of the structure itself, he stated: "Oh, no." (R. 102).

Finally the Petitioner produced the testimony of Mr. Wayne C. Evans, an account executive with David W. Evans & Associates. He stated that there is only one advertising media of which the customer takes possession. This is the so-called "gimmick" such as fountain pens or balloons and the like. (R. 105). With regard to all other media, including television, radio, newspaper, and outdoor billboards, he stated that his clients "never" take possession of the personal property or media involved (R. 105). He also noted that the only purpose for the use of any of their media, including outdoor billboards, is "to communicate the idea to the maximum number of people at the minimum cost." And finally, with regard to possessory or proprietory interest of the outdoor signs, he stated as follows:

> "We have nothing physically to do with structure or ownership matter. This is all handled by the outdoor company. We contract with them to reach a number of people through their locations and signs." (R. 106).

The auditing division of the Tax Commission produced no testimony whatsoever to controvert the foregoing evidence as to the nature of the transactions of plaintiff and its various advertising clients.

Decision of the Tax Commission.

After the hearing had been completed, and each of the parties had submitted post-hearing memoranda, the Tax Commission promulgated a decision under date of October 25, 1966. The "findings of fact" of such decision (R. 204) consist primarily of a repetition of certain stipulated facts contained in the stipulation by the parties. (R. 10). There were no findings of facts made with regard to the critical

issues in this case concerning possession, use, whether or not the transaction involved a lease of tangible personal property, etc. Rather, in the "conclusions of law" (R. 205), the Commission simply went down the list and found as a matter of law that:

(1) The painted billboards involved are "tangible personal property."

(2) The plaintiff's clients acquire "the right of continuous possession" of the painted billboards.

(3) Clients of plaintiff acquire "the right of continuous use" of the painted billboard.

(4) Such transfers would be taxable if they were an outright sale.

(5) In actuality, plaintiff's clients exercise a proprietory interest in and a control over the billboards.

(6) The transaction is taxable under §59-15-2 (g) *Utah Code Annotated,* 1953.

It should be noted that the so-called "conclusions of law" are in actuality factual determinations of ultimate facts in this matter. There were no findings of fact made by the Commission to create a connective thread between the testimony and the stipulation before the commission to its ultimate decision. The Commission did not list its reasons, its theories, or its interpretation or analysis of the facts, but merely listed several ultimate legal conclusions.

A petition for re-hearing was filed by plaintiff on the 14th day of November, 1966, and was denied under date of December 30, 1966.

ARGUMENT

POINT I

THE PROVIDING OF ADVERTISING SPACE ON A BILLBOARD IS NOT WITHIN THE LEGITIMATE AMBIT OF SALES TAXATION UNDER *UTAH CODE ANNOTATED*, §59-15-2(g).

Before analyzing, with particularity, the specific advertising arrangement between Plaintiff and its clients, it would be well to review the basic legislative and administrative framework under which the Commission here seeks to impose sales taxation.

The Commission does not claim in this proceeding that Plaintiff actually "sells" anything to its customers, but attempts to come within the language of *Utah Code Annotated* §59-15-2(g) (1953):

> "When right to continuous possession or use of any article of tangible personal property is granted under a lease or contract and such transfer of possession would be taxable if an outright sale were made, such lease or contract shall be considered the sale of such article and the tax should be computed and paid by the vendor upon the rentals paid."

Statutes like this have been enacted in most states which have a sales tax. The purpose of such legislation, originally, was to plug a loophole which had developed whereby persons would evade the sales tax by disguising a sale in the form of a "lease." Thus, for example, an automobile might have been "leased" for a ten year period at a "rental" which, in fact, constituted the sale price of the vehicle

amortized over a long period of time. Such subterfuge became sufficiently common that corrective legislation in the form of statutes like §59-15-2 (g) was enacted to curb the problem.

Thus, in interpreting such statutes, the Courts have referred back to their original purpose and many have held that only those "leases" which create the normal incidents of a sale should be taxed. Bona fide rentals, not made with an intent to evade sales tax, have been held not to be taxable. See, *U-Drive-Em Service Co. v. State,* 204 Ark. 501, 169 S.W.2d 584 (1943); *Watson Industries v. Shaw,* 235 N.C. 203, 69 S.E.2d 505 (1952).

The interpretation employed should depend ultimately upon the applicable legislation or regulation which, in Utah, leave little doubt as to the proper scope of taxation. The statute itself requires that the lessee receive the *continuous* possession or use of the property involved. Since it must be assumed that the legislature intended something by the use of this term, the logical conclusion is that it intended to tax only those alleged "leases" which, because of their continuous term, were tantamount to sales of the property involved.

Any doubt about this has been resolved by the Tax Commission's regulation S-32 which provides for the taxation of only those leases made "in lieu of outright sales." Clearly, this phraseology would limit the tax to those situations where through a "lease," a buyer obtains virtually all of rights of "possession" and "use" as would result from an outright sale. The phrase is not novel to tax legislation and it can only be assumed that the Commission was aware of the effect of including such terminology. In *Universal*

Engineering Co. v. State Board of Equalization, 256 P.2d 1059 (Cal. 1953), for example, the Court considered a statutory provision taxing leases made "in lieu of sales." In construing this language, the Court concluded that only those leases during which the property was "substantially consumed" would be taxable. This, again, results in taxing only "rentals" which permit the same general "possession" and "use" as would an outright sale.

The only Utah case which has interpreted *Utah Code Annotated* §59-15-2(g) deals with just a transaction. In *Young Electric Sign Co. v. Utah State Tax Commission,* 4 Utah 2d 242, 291 P.2d 900 (1955), the Court considered a "lease" of signs wherein the "rental" was based upon the cash sales price of the sign. Moreover the sign company there wrote the sign off as an asset after the original term of the lease. This transaction had all the earmarks of a sale except for the passage of title, and the Court thus held that the transaction was taxable. We submit that this was a proper application of the tax to a lease made "in lieu of an outright sale."

The instant case presents a factually different and legally distinguisable transaction. The advertising agreement between Plaintiff and its customers has none of the aspects of a sale. Indeed, it is not even a lease, but rather an agreement whereby Plaintiff agrees to place the customer's message before the public. This is a wholly different type of a transaction — a square peg, as it were, which the Tax Commission has now tried to torture into the round hole presented by §59-15-2 (g) and Regulation S-32. Neither the essence nor any significant facet of the transaction involves the transfer of possession of tangible per-

The various advertising witnesses were in accord that they had no interest whatsoever in the sign structure itself. (R. 35, 54, 56, 61, 92, 96, 102 & 106). Their purpose in dealing with Plaintiff was stated to be the same as in their arrangements with other advertising media such as television, radio, newspapers, etc. (R. 105, 92, 35).

The comparison to other media is persuasive. With regard to television, newspapers, radio and billboards, the purpose is the same — to reach a given segment of the public. In each transaction there is personal property involved as a means to this desired end — video tape, printer's mats, audio tape, copy, or a billboard structure. Such property is not, however, the essence of the transaction but merely an incidental step toward the desired results. Just as a doctor must use his surgical tools to cure and a lawyer must use law books, typewriters and paper to properly serve his client, so must the various advertising media, including Plaintiff, use personal property in serving their customers' needs.

It will doubtless be argued by Defendant that the "purpose" of an agreement is not relevant in determining its taxability. Defendant has previously illustrated this argument by stating that two persons could not agree that a horse is, in fact, a cow in order to evade a horse tax. We would agree, but submit that the keystone to any such analysis must be good faith. There has been no suggestion that Plaintiff here seeks to evade taxation by spuriously misnomering its transaction. To the contrary, the actual facts of the arrangement support and bear out the proposition that is simply not a property transaction.

Another most significant fact is that there is no transfer of possession of the billboard to the advertiser. This will be amplified in a subsequent point, but the evidence, in total, demonstrates unequivocally that the client receives no significant possessory rights or interests. To the contrary, the Plaintiff retains the obligations to repair, maintain, re-paint and re-locate the sign structure. The client merely receives a contractual right to have his message put before the public.

Perhaps the clinching fact and best evidence is found in the Tax Commission's own regulations and actions. The Commission is, of course, the designated expert in interpretation and administration of this state's tax structure. In Regulation S-65 the Commission has provided:

> "Advertising space sold in newspapers, magazines, *or otherwise* is not subject to tax. Likewise, charges made by advertising agencies for preparing and placing advertising media are charges for service and, therefore, are not taxable." (Emphasis ours.)

The concluding paragraph of the Regulation provides:

> "The tax does not apply with respect to art work produced with the office of the advertiser or the advertising agency for the purpose for visualization of any idea and the client's selection of the particular visualization he favors for use in his advertisements. The sale of materials to the advertiser or advertising agency for producing such art work is subject to tax."

The evidence undisputedly shows that Plaintiff's clients are purchasing "advertising space," just as would be done in a magazine, on the back end of a city bus, or in a newspaper.

That is the essence and totality of the agreement. Not only the Regulation itself but the Commission's long-standing interpretation thereof support this exception. Although §59-15-2(g) has been in existence for some 30 years. (See, *Laws of Utah* 1935, ch. 91 §1), the first attempt by the Commission to tax outdoor advertising receipts did not occur until 1963. (R. 10). It logically follows that until 1963, the Commission itself had considered outdoor advertising receipts to be exempt under Regulation S-65. Now, by some unknown ledgerdemain the Commission seeks to reverse its long-standing interpretation, erase S-65 from the books, and torture §59-15-2(g) into application. The Commission should not be allowed to thus disclaim its own Regulation and interpretation, for as has been noted by this Court:

> "Long compliance with an administrative ruling lends strength to the proper presumption of the regulation's validity." *Utah Concrete Products Corp. v. State Tax Commission,* 101 Utah 513, 125 P.2d 408 (1942).

Nor should the Commission be permitted to limit the obvious and accepted effect of S-65 by applying the cryptic doctrine of *ejusdem generis* to the terms "or otherwise." Not only would this be inconsistent with the Commission's past actions, but also it would contravene the equally applicable maxium that ambiguous tax measures should be construed in favor of the taxpayer and strictly against the taxing authority. *Utah Farm Bureau Ins. Co. v. State Tax Commission,* 9 Utah 2d 421, 347 P.2d 179 (1959).

A significant aspect of the Commission's action is that it evokes a considerable discrimination aaginst advertisers

vis a vis other media with which the outdoor people compete. The evidence demonstrates that outdoor advertising is in direct competition with television, newspapers, and magazines. The equilibrium which has existed for many years when none of the media were taxed would be abruptly altered by the imposition of tax against only outdoor advertising. In this regard, the Commission has stipulated that it has not attempted to and does not now seek to impose a tax upon the other media. (R. 11).

Such rank discrimination, such abrupt departure from 30 years of uninterrupted practice, and such a clear deviation from both the intent and wording of the applicable legislation and regulation should not be permitted by this Court.

POINT II

THE FINDING OF THE COMMISSION THAT CLIENTS OF PETITIONER ARE GRANTED A RIGHT TO CONTINUOUS POSSESSION AND USE OF THE OUTDOOR SIGNS IS CLEARLY ERRONEOUS.

This matter is before this Court under the provisions of *Utah Code Annotated* §59-15-14 (1953) which provides that review by the Court may be "both upon the law and the facts." Although the Court has accorded to the Tax Commission some latitude with respect to the determination of factual issues (See *Butler v. State Tax Commission*, 14 Utah 2d 1, 367 P.2d 52 (1962)), such latitude does not constitute a *carte blanche* by which the Commission may act in disregard of material facts or draw unwarranted conclusions from the facts before it. In all events, the Com-

mission is bound by the applicable law and it may not make findings of fact which effectually alter such legislative framework. See *Western Leather and Finding Company v. State Tax Commission,* 87 Utah 227, 48 P.2d 526 (1935), where this Court noted that the power vested in the Tax Commission "does not vest in the Commission any discretion whatsoever in the matter of requiring a payment of a sales tax by anyone other than such as are designated in the act."

Even assuming *arguendo* that the instant transaction were within the sphere and intent of §59-15-2(g), which we submit it is demonstrably not, the Commission has erred in making certain factual findings, critical to the question of taxation. The foremost of these is the Commission's finding concerning possession herein. As has been noted, the statute prescribes the following criteria for taxation:

> "When the right to *continuous possession or use* of any article of tangible personal property is granted under a lease or contract and such *transfer of possession* would be taxable if an outright sale were made, such lease or contract shall be considered the sale of such article and the tax shall be computed and paid by the vendor or lessor on the rentals paid."

The Commission, itself, in Regulation S-32, has amplified the need for finding of possession as follows:

> "Tax on receipts of leases and rentals applies when the lessee has the right to *use and operate* the tangible personal property."

Thus, possession is the *sine qua non* of taxation under §59-15-2(g).

With regard to such key factors, the Commission made the following conclusions:

> (2) "Clients of petitioner acquire under provisions of the contracts and the agreements entered into with petitioner the right of continuous possession of the painted billboard involved.
>
> (3) "Clients of petitioner acquire under the provisions of the contracts and agreements entered into with petitioner the right of continuous use of the painted billboard involved.
>
> (5) "In the actual operation of the contracts and agreements involved, the clients of the petitioner, Snarr Advertising, Inc., exercised a *proprietory interest in and control over* the painted billboards in question." (R. 206). (Emphasis ours.)

It will be noted that these so called "conclusions of law" are essentially findings of utimate facts. It is significant that the decision of the Commission does not contain its reasons, its analysis, or its discussion of the transaction involved. Rather, the "conclusions" simply parrot the statutory language in blunt conclusions, wholly unsupported by and unconnected to the evidence.

The facts in this matter, largely undisputed, clearly illustrate that any connection between the evidence and the Commission's findings as quoted above is purely coincidental. Without exception, the witnesses testified that as clients of plaintiff they had nothing whatsoever to do with the actual sign structure itself. They do not maintain the structure, exercise control over it, move it, paint

it, alter it, or deal with it in any way. Significantly, the advertising clients have no interest whatsoever in even the real property upon which the sign structures are located. To the contrary, such property is leased directly to Plaintiff by the land owner, and in such lease Plaintiff is given the sole right to enter upon such property. (R. 199). Therefore, the advertising clients cannot even gain entry to the sign structure without committing a trespass as against both Plaintiff and the landowner.

On the other hand, Plaintiff, itself, retains the control over the sign structure. Plaintiff has the obligation to maintain the signs, re-paint them, repair them, move them in the event that the original location becomes undesirable for advertising purposes, and Plaintiff maintains the sole right to go upon the real property where such signs are located.

The Commission did not specify what rights of possession were granted to the advertisers by Plaintiff. And indeed a review of the evidence, the contract (R. 203) and the lease agreement between the Plaintiff and the land owner (R. 199), compels the conclusion that there are no possessory rights granted to the advertiser. In light of the facts, and the law which will be discussed hereinafter, the Commission's findings evoke a new concept of "possession" which is novel to and a perversion of several hundred years of Anglo-Saxon property law.

The only case dealing with §59-15-2(g) is *Young Electric Sign Co. v. State Tax Commission.* This case sheds no light on the possession problem, however, since there was simply no question raised there concerning possession.

The taxpayer conceded that it had to pay a tax on at least part of the rentals received and thus conceded that possession was transferred. In any event, that case is so variant from the instant one on the facts that it would have no precedential value here. The signs there were custom-made identification signs installed on the premises of the customer. The contract, as previously noted, was essentially a sale. Thus, *Young* gives no assistance one way or the other in the instant case.

There are, however, several cases from other jurisdictions, interpreting similar statutes, to which Plaintiff would invite the Court's attention. A case closely in point is *Federal Sign & Signal Company v. Bowers,* 172 Ohio St. 161, 174 NE2d 91 (1961), which dealt with the taxability of outdoor electric sign display transactions. The statute there imposed a sales tax on transactions in which "possession . . . is or is to be transferred." Similarly, the Utah statute refers to "a right of continuous possession" but also refers to "such transfer of possession" — indicating an actual, past-tense transfer. The sole question in *Federal Sign* was whether the transaction involved a transfer of possession, and the Court adopted the following reasoning of the Board of Tax Appeals:

> "In none of the appellant's transactions was 'title' to the signs transferred. In some of its transactions neither 'title' nor 'possession' of the signs was transferred. In the other transactions, such as the ones here in question, the only 'possession' that was transferred to the customer was the 'formal possession' made necessary by virtue of the fact that the signs were erected on real property owned or leased by the customer rather than on property owned or leased by appellant. However, by virtue of

> the provisions of the rental agreements, the appellant at all times retained the 'possession' or 'custody' necessary to perform the maintenance on these signs required under the terms of the agreements. And the signs themselves were not used or manipulated in any way by the customer in the same sense that a rented automobile, business machine, etc., might be said to be so used."

The Court thus sustained the non-taxability of the advertising transaction. The advertising agreements in the instant case are identical to those discussed in *Federal Sign* since Plaintiff retains the right and obligation to repair, maintain, and re-locate the signs as is necessary. The only distinction between the cases is that in *Federal Sign,* the signs were located on the property of the customer in some instances — which, of course, would be a possessory right absent from the instant transaction.

Also of pertinence is the discussion of the Supreme Court of Colorado in *Herbertson v. Cruise,* 115 Colo. 274,170 P.2d 531 (1946) which involved exactly the same statutory language as we have in §59-15-2(g). In construing the term "continuous possession," the Court concluded:

> "It seems apparent that the most clear cut example of what the law is intended to reach is the case of the calculating machine or multigraph machine *in place of the lessee's business,* and supervised by lessor under a rental agreement covering a continuous (and usually a very considerable) period of time. This involves a more permanent type of lease than a multifarious type, renting driver-less cars for their varied purposes, where it might well happen that thirty different persons, have the rental service of the same car. In the former case, the lessee is securing the *most permanent title* that the

non-selling policy of the lessor allows him to acquire." (Emphasis ours.)

Under such reasoning and the facts of the instant case where the client never assumes possession, control or a proprietory interest in the property involved, continuous possession is clearly not shown.

Of similar import is the case of *Ford v. Oklahoma Tax Commission,* 285 P.2d 436 (Okla. 1955). The statute in that instance provided that "the term 'sale' is hereby declared to mean the transfer of either the title or possession of tangible personal property. . ." Thus, the statute requires somewhat less than ours since it mentions nothing about "continuous" possession. The Court was called upon to define possession, and concluded as follows:

> "In *Webster's New International Dictionary,* Unabridged, 2nd Edition, definitions of the word 'possession' are as follows:
>
> > 'Act or state of possession . . . law. Act, fact, or condition of a person's having such control of property that he may legally enjoy it to the exclusion of all others having no better right than himself.'
>
> "The word 'possess' is stated as meaning 'to have and hold as property, to have a just right to; to be master of . . .'
>
> "Under all circumstances in its connection with tangible personal property, *the otherwise unmodified word 'possession' clearly refers to him who has actual physical control of the thing and conveys a clear and definite meaning.*" (Emphasis ours.)

Under this rationale, in all fairness, it cannot be said that the advertising clients in the instant case have "actual physical control of a thing."

In New York City, the sales tax statute applies to "any transfer of title or possession or both." The New York Court of Appeals, in construing this provision, has held that it requires the transfer of "actual, exclusive possession." *American Locker Company v. City of New York,* 308 NY 264, 125 NE2d 421 (1955). In the same case it was noted that "constructive possession" was insufficient.

A further note should be made concerning the word "use" as it appears in the statute. The statute requires "continuous possession or use," but goes on to refer to "such transfer of possession." It would appear that "use" was intended to be something not dissimilar to "possession" — otherwise, of course, the Legislature would have said "such transfer of possession *or use.*" There are relatively few sales tax statutes which employ the word "use" and we have found but one case discussing the term in this context. In *Howitt v. Street & Smith Publications,* 276 NY 345, 12 NE 2d 435 (1938) the Court defined "use" as follows:

> "We believe that the ordinary interpretation of the word 'use' is to assert possessory interest in the article for some length of time. . . Anything less than this, as merely the right to reproduce, is not such a use as should make the transaction taxable as a sale of taxable personal property."

The Utah State Tax Commission has accorded "use" a similar construction in Regulation S-32 which says, in part:

> "Tax on receipts from leases and rentals applies when the lessee has the right to *use and operate* the tangible personal property."

It is submited, therefore, that the word "use" adds little to the term "possession" and that the two, in this context, have similar meanings. The mere fact that the Legislature used two words instead of one does not necessarily preclude giving the two terms similar meanings. (See *Utah Concrete Products Corp. v. Tax Commission*, 101 Utah 513, 125 P.2d 408 (1942) where the Court construed "used" and "consumed" as having the same meaning even though used together in the statute.) Certainly the term "use" contemplates control, and the right to consume, alter, vary or manipulate the article involved, such rights being demonstrably absent here.

Both "possession" and "use" are modified in the statute by the term "continuous." In this regard, it should be noted that Plaintiff's cilents do not gain any rights in a given structure which are "continuous" for, in all events, Plaintiff maintains the right to re-locate or replace any specific structure should its advertising value be changed.

In summary, therefore, the facts in this case are such as to make the Commission's findings in this regard clearly unreasonable and erroneous. The *Young Electric* case clearly does not support such findings since it does not discuss "possession." Moreover, the cases from other jurisdictions dealing with analogous or identical statutes do not in any way bolster the Commission. To the contrary, if "possession" and/or "use" are found to exist in this case, it would constitute a broader scope of taxation than has been sanctioned by any Court which has considered the problem.

POINT III

THE TRANSACTION BETWEEN PLAINTIFF AND ITS CUSTOMERS CONSTITUTES THE SALE OF A NON-TAXABLE SERVICE.

Plaintiff has devoted the preceding two points of argument to the propositions that the advertising transaction here involved is not within the intended sphere of §59-15-2(g) and that, in any event, no right to possession is transferred to the customers in the transaction. Even if we were to assume, *arguendo,* that this is generally the type of transaction intended to be taxed and, further, that possession is transferred (neither of which assumption can be made on the record here involved), Plaintiff nonetheless submits that the transaction here involves the sale of a non-taxable service under the previous holdings of this Court.

To analyze this contention properly, it is necessary to view the "totality" of the transaction between Plaintiff and its customers. We have pointed out above that the purpose of the transaction is not the transfer of property, but the provision of an advertising service through outdoor signs. The parallel between outdoor signs and other advertising media has also been discussed. The testimony demonstrates that there are numerous aspects of the transaction which are essentially unrelated to the sign strucure itself. Plaintiff acquires real property for sign locations, it develops artistic ideas and advertising presentations, it arranges for the electrification and re-location of the signs, and it repairs and maintains the signs.

The allocation of cost involved is of key importance in this regard. Plaintiff's comptroller testified that the sign structure itself is not particularly significant in determining the cost to the customer. (R. 70). Matters such as the location, length of service, maintenance and acquisition of property were cited as being the principle criteria for the price charged.

On a typical sign structure, the cost to the customer would run $1600 for a four year period. (R. 71). Of this income, approximately 15% would be allocable to: materials (5%), labor in painting and preparing sign (5%) and placement of the sign (5%). (R. 71 and 75). The remaining 85% of the income is allocable to the various other services mentioned above. (R. 75). It is undisputed that services, per se, are untaxable,* as is the real property provided. As for the materials themselves, Plaintiff purchases its paint, lumber, nails, etc. as an ultimate consumer and had in the past paid a sales tax on such items at that time. (R. 167 — notes from a member of the auditing staff). This again points out the basic inconsistency in the Commission's position here. The Commission has had no hesitancy in collecting sales tax on the materials purchased by Plaintiff, nor has the Commission protested when the tax was paid for repairs under §59-15-4(e). Now, however, it seeks to have its cake and also eat it by claiming a tax on the *entire proceeds* from the advertising agreement — apparently on the theory that the revenues would be greater than those derived from the previous method of taxation. Clearly, if the Commission should succeed in this question-

*With the exception of services in repair of property for which Plaintiff pays taxes under Utah Code Ann. §59-15-4(e)(1965).

able effort, Plaintiff would be entitled to a refund on all taxes paid heretofore on either materials or repairs.

The net result of the present arrangement is clear. The Commission seeks to impose a tax on 100% of income notwithstanding the facts that 85% of the income is allocable to non-taxable services (or services for which taxes had previously been paid) and 15% is allocable to the sign itself, with a tax already having been paid in at least 5% of this (prior to the audit here involved). The remaining 10% allocable to the sign is labor expense in painting and placing the sign, and it can be seriously questioned whether this is taxable in light of the fact that it can only be tied in with materials already taxed.

Even giving the Commission the benefit of the doubt, the best that can be said is that 15% of the total proceeds (not otherwise taxed or otherwise exempt) are arguably allocable to the sign structure. We submit that under the decisions of this Court this is insufficient to bring the transaction within the legitimate sphere of taxability.

This Court has held that where the property involved in a transaction is merely incidental to a service rendered in conjunction therewith, the transaction is not taxable. See *Young Electric Sign Company v. Utah State Tax Commission,* 4 Utah 2d 242,291 P.2d 900 (1955), *Western Leather and Finding Company v. Utah State Tax Commission,* 87 Utah 227, 48 P.2d 526 (1935). In *Young,* the Court held that "repair sales" were primarily services with the materials involved being "merely incidental." Thus, the transaction was held not to be taxable. The percentage which materials bore to the total income on such transaction was

12% (6% cost marked up 100% for retail). The Court discussed the matter as follows:

> "Whether this is stated one way or the other, the substance is the same, and our problem is to determine whether these were sales of materials under the Act, or whether the furnishing of materials was merely incidental to the furnishing of services for which the charge to the customers was actually made. What the customers were obtaining from the companies were principally services and not goods. The customers did not obtain the right of possession or use of the sign as a result of such repair; they were the owners of the signs before the repairs were made. In our opinion, it would be unreasonable to find under these conditions that the materials represented a substantial portion of the outlay, and that their use was more than merely incidental to the services rendered. The Commission erred in assessing taxes on "repair sales."

The evidence here brings Plaintiff to a comparable percentage — some 15% of income being possibly allocable to the sign structure.

The Commission will no doubt argue at this juncture that *Young Electric* precludes this type of an argument with regard to a "lease." Plaintiff would first point out that *Young* is so vastly distinguishable from this case, to the extent that it deals with leases, that it has no precedential value here whatsoever:

> (a) In *Young,* the "lease" had all of the earmarks of a sale — indeed the sign itself was paid for during the term of the agreement and the sign company wrote it off as an asset.

(b) In *Young,* the price was based upon the fair cash value of the sign.

(c) In *Young,* the percentage of materials was 50% of the receipts.

(d) In *Young,* possession was transferred.

None of these facts apply to the instant transaction. Therefore, the holding of *Young* with respect to the rental questions therein really has no application.

In any event, Plaintiff respectfully submits that one aspect of the *Young* decision would be unsound if applied to the facts of this case. The Court seemed to say in *Young* that leases, as opposed to sales, may not be analyzed to determine whether they are in reality services, with the property involved being incidental thereto. Relying on the language in §59-15-2(g) which provides that taxes should be computed upon the "rentals paid,"* the Court noted:

> "What elements enter into the charges for these rentals can be of no materiality."

As noted above, such language is inapplicable here because of the factual differences involved. Notwithstanding this, Plaintiff would submit to the Court that a transaction sought to be taxed under §59-15-2(g) can and should be exempted if it is essentially a service. Certainly, an outright *sale* incident to a service is exempt (See *Young Electric v. Utah State Tax Commission, supra,* and *Western Leather and Finding Company v. Utah State Tax Commission, supra*) and the same treatment must be accorded to a non-

*It is not clear why this should give §59-15-2(g) transactions any different posture than actual sales, since the section dealing with the latter provides for a tax to be computed on "the purchase price paid or charged." Utah Code Ann. §59-15-4(a).

sale under this section. The statute, §59-15-2(g), unequivocally contemplates that sales and possession transactions must be treated exactly the same for tax purposes. Note that the statute provides that the only "leases" to be taxed are those which would be taxed if they were an "outright sale." Therefore, to discriminate against leases in any way, as opposed to outright sales, would be to contravene the clear wording of the statute itself. It follows that since sales are non-taxable, if merely incidental to a service, such should be the case with transactions under §59-15-2(g). If *Young* were construed to hold to the contrary, it should be overruled.

A more recent Utah case dealing with the "property"-"services" distinction is *McKendrick v. State Tax Commission*, 9 Utah 2d 418, 347 P.2d 177 (1949), where the Court held that the sale of artificial limbs was primarily a sale as opposed to a service, and taxation was sustained. The Court there said:

> "The exact allocation of the cost of labor and materials is not controlling. It is the synthesis of both in the finished product which determines its sales value." (9 Utah 2d 420).

Thus, where the cost of materials was equal to one-half the cost of labor, all of which were represented in the final product of an artificial limb, the Court sustained taxation. As noted in the opinion, the same reasoning would apply to a pound of ore worth but a few cents but fashioned ultimately into hair springs for watches worth thousands of dollars.

The instant case, however, is distinguishable from these examples, as might be best illustrated graphically:

Labor	5%	15% represented in value product itself
Materials	5%	
Placement of sign	5%	
Lighting		85% not represented in final value of product.
Repair		
Maintenance		
Re-location		
Land Acquisition		
Artistic Services		
Creation of Advertising Ideas		

The distinction is, in the words of this Court in *McKendrick,* in "the synthesis . . . in the finished product." In *McKendrick,* in the watch spring example, and in many of the hypotheticals which will no doubt be employed in the Attorney General's Brief, the labor and services all enhance the basic value of the personal property and thus are an integral and inseparable part of it. In the instant case, it was noted to the contrary that the value of the sign structure is not enhanced by the various services for they are not services applied directly to the improvement of the property but to tangential aspects of Plaintiff's total advertising program.

It is pertinent to refer again to Regulation S-65 wherein the Tax Commission has stated that advertising space agreements are *services* rather than property and thus should not be taxed. For some 30 years this has been applied to billboards and we question the right of the Commission to now reverse itself in midstream, without amendment to the legislation.

It is submitted, therefore, that as a matter of law, under the undisputed facts herein, the Commission erred

in finding that this was a lease of tangible personal property subject to taxation. To the contrary, under the *Young Electric* decision, the instant transaction would constitute the sale of a non-taxable service.

CONCLUSION

In summary, Plaintiff submits respectfully that the decision of the Tax Commission herein should be reversed as a matter of law for the following reasons:

(a) The advertising transactions here in question do not come within the intent or wording of *Utah Code Annotated,* §59-15-2(g). This is best illustrated by the nature of the transaction itself, by the 30 year history of non-taxation, and by the terms of the Tax Commission's own regulation S-65, which clearly exempts this transaction.

(b) That, in any event, the Commission erred in finding that clients of Plaintiff are granted rights to use or possession of the signs involved. Even under the most favorable interpretation, the evidence simply does not support such conclusions, and the Tax Commission has thus transcended its fact-finding discretion.

(c) That the transaction between Plaintiff and its clients is essentially the sale of a service and any tangible personal property involved therein is merely incidental to such services — thus, the transaction is untaxable.

Plaintiff submits that the action of the Commission herein is so demonstrably unfair and discriminatory, is so clearly a perversion of the legislative intent and the normal

legal concepts of taxation and property law, and is so abrupt a reversal of the Commission's long-standing practice, that it cannot be sanctioned by this tribunal.

Respectfully submitted,

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